

**STATE OF WASHINGTON
OFFICE OF THE INSURANCE
COMMISSIONER**




**FINANCIAL EXAMINATION
OF
Lutheran Bible Institute of Seattle
Issaquah, Washington
AS OF DECEMBER 31, 2003**

Lutheran Bible Institute of Seattle
Order No. G04-74
Exhibit A

CHIEF EXAMINER AFFIDAVIT

I hereby certify I have read the attached Report of the Financial Examination of Lutheran Bible Institute of Issaquah, Washington. This report shows the financial condition and related corporate matters as of December 31, 2003.


Patrick H. McNaughton
Chief Examiner

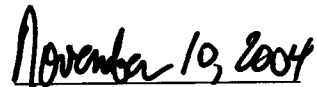

Date

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SALUTATION

Seattle, Washington
October 28, 2004

The Honorable Mike Kreidler, Commissioner
Washington State Office of the Insurance Commissioner (OIC)
Insurance 5000 Building
5000 Capital Blvd.
Tumwater, WA 98501

Dear Commissioner Kreidler:

In accordance with your instructions and in compliance with the statutory requirements of Chapter 48.38 RCW, Charitable Gift Annuity Business, an examination was made of the corporate affairs and financial records of

Lutheran Bible Institute of Seattle

of

Issaquah, Washington

hereinafter referred to as "LBIS" at the location of its home office, 4221 228th Avenue SE, Issaquah, WA 98029.

This report of examination is respectfully submitted showing the condition of LBIS as of December 31, 2003.

SCOPE OF THE EXAMINATION

This examination covers the period January 1, 1999 through December 31, 2003. The examination was conducted in accordance with statutory requirements contained in the Revised Code of Washington (RCW) and the guidelines recommended by the National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook. We focused our review and testing on LBIS' management, operations, and reporting of the charitable gift annuity business as considered necessary to ascertain the financial condition of the organization and conformity with the related laws. These matters are discussed in this report. The examination was conducted at the Issaquah office of LBIS by examiners from the state of Washington.

LBIS records along with various aspects of the organization's operating procedures and financial reports were reviewed and tested during the course of this examination and are commented upon in the following sections of this report. In addition, the organization's certified public accountant's (CPA's) reports were reviewed and utilized, where possible, to facilitate efficiency in the examination.

INSTRUCTIONS

The examiners reviewed LBIS' Annual Reports as part of the statutory examination. This review was performed to determine if the organization completed the Annual Reports in accordance with the Annual Report Instructions published by the OIC and to verify that the organization's accounts and records were prepared and maintained in accordance with Chapter 48.38 RCW.

The following summarizes the exceptions noted while performing this review.

1. 2003 Annual Report - Annuities Payable/Reserves

The reported annuities payable, amounting to \$737,325, were understated by \$38,765 as of December 31, 2003. LBIS did not account for the actuary's calculated reserve amount plus a ten percent (10%) of the calculated reserve, as required by RCW 48.38.020(1) and (3). Consequently, the understated liability resulted in overstating the temporarily restricted net assets by \$38,765.

RCW 48.38.020 and states that:

- (1) "Upon granting to such insurer or institution under RCW 48.38.010 a certificate of exemption to conduct a charitable gift annuity business, the insurance commissioner shall require it to establish and maintain a separate reserve fund adequate to meet the future payments under its charitable gift annuity contracts."
- (3) "The amount of the separate reserve fund shall be:
 - (a) For contracts issued prior to July 1, 1998, not less than an amount computed in accordance with the standard of valuation based on the 1971 individual annuity

- mortality table with six percent interest for single premium immediate annuity contracts and four percent interest for all other individual annuity contracts;
- (b) For contracts issued on or after July 1, 1998, in an amount not less than the aggregate reserve calculated according to the standards set forth in RCW 48.74.030 for other annuities with no cash settlement options;
 - (c) Plus a surplus of ten percent of the combined amounts under (a) and (b) of this subsection."

LBIS is instructed to report the statutory reserve amount on its financial statements in compliance with RCW 48.38.020(1) and (3).

2. 2003 Annual Report - Minimum unrestricted net assets

LBIS' Annual Report and accounting records showed an unrestricted net assets balance of \$14,856 as of December 31, 2003 which was significantly below the minimum unrestricted net assets amount. The 2002 Annual Report also reported an unrestricted net assets balance of \$394,628. LBIS, therefore, did not comply with RCW 48.38.010(6) because it did not maintain the required \$500,000 minimum unrestricted net assets during the periods 2002 and 2003.

RCW 48.38.010 states that, "The commissioner may grant a certificate of exemption to any insurer, or educational, religious, charitable, or scientific institution conducting a charitable gift annuity business: (6) Which has and maintains minimum unrestricted net assets of five hundred thousand dollars."

LBIS is instructed to maintain, at all times, the required minimum unrestricted net assets to ensure its compliance with RCW 48.38.010(6).

3. 2002 Annual Report – Assets of the separate reserve fund

The 2002 Annual Report was inaccurate. The fund balance of \$751,866 reported in the Charitable Gift Annuities Reserve Fund Activity Statement did not agree with the total investments of \$623,018 reported by the investment managers. Also, we found that as of December 31, 2002, the annuity assets or investments were significantly below the statutory annuity reserves or liabilities by \$128,848. As a result, LBIS was not in compliance with RCW 48.38.010(10)(a) and RCW 48.38.020(1) and (2)(b). The assets of the separate reserve fund were inadequate, as of December 31, 2002, to meet payments under its charitable gift annuity contracts. The OIC was not able to determine the inadequacy of the annuity assets in a timely manner because the 2002 Annual Report submitted by LBIS did not appropriately disclose the actual annuity investments balance as of December 31, 2002.

RCW 48.38.010 states that: "The commissioner may grant a certificate of exemption to any insurer or educational, religious, charitable, or scientific institution conducting a charitable gift annuity business: (10) Which: (a) Files with the insurance commissioner

on or before March 1 of each year a copy of its annual statement prepared pursuant to the laws of its state of domicile, . . . ”

RCW 48.38.020 and states that:

- (1) “Upon granting to such insurer or institution under RCW 48.38.010 a certificate of exemption to conduct a charitable gift annuity business, the insurance commissioner shall require it to establish and maintain a separate reserve fund adequate to meet the future payments under its charitable gift annuity contracts.”
- (2) “The assets of the separate reserve fund: (b) Shall be invested in the same manner that persons of reasonable prudence, discretion, and intelligence exercise in the management of a like enterprise, not in regard to speculating but in regard to the permanent disposition of their funds, considering the probable income as well as the probable safety of their capital. Investments shall be of sufficient value, liquidity, and diversity to assure the insurer or institution’s ability to meet its obligations.”

To comply with RCW 48.38.010 and RCW 48.38.020, LBIS is instructed to:

- **Maintain, at all times, annuity assets or a separate reserve fund adequate to meet the future payments under its charitable gift annuity contracts;**
- **Develop and implement a system for accounting, investing, and reporting of its charitable gift annuity business to ensure compliance with the principles or practices prescribed or permitted by Chapter 48.38 RCW; and**
- **Develop and implement procedures for appropriate review, by staff other than the report preparer, to ensure completeness and accuracy of the Annual Report.**

COMMENTS AND RECOMMENDATIONS

1. Annuity Agreements

There were instances wherein information in the annuity agreements, such as the annual payment amount or the present value of annuity, did not agree with the charitable gift annuity spreadsheet. The spreadsheet, which supports the annuity agreement, includes calculations and information such as donor’s name, birth date or age, amount transferred, gift date, payment frequency, annual annuity payout, present value of annuity, charitable gift value, and others.

It is recommended that LBIS make the necessary revisions and record the correct annual payment amounts and/or reasonable commensurate value of the benefits in the annuity contracts to agree with the charitable gift annuity spreadsheets.

COMPANY PROFILE

History: The Lutheran Bible Institute of Seattle (LBIS) began operations in 1944 and became an independent nonprofit corporation registered with the state of Washington in 1959. Trinity Lutheran College (LTC), a registered trade name of LBIS, is a private college accredited by the Northwest Association of Schools and Colleges.

Territory and Plan of Operation: Trinity Lutheran College, also known as LBIS, maintains a program of biblical studies at the collegiate level. The program trains and prepares students for optimum stewardship of their lives in church vocations worldwide or in whatever vocations they choose.

LBIS was granted a Certificate of Exemption Number 137 to conduct a Charitable Gift Annuity business in the state of Washington by the OIC on March 17, 2000. LBIS was originally issued a Certificate of Exemption to issue charitable gift annuities on July 30, 1980. The original Certificate of Exemption was revoked on July 7, 1981 because LBIS did not comply with the provisions of Chapter 48.38 RCW. There were 68 in-force annuity contracts as of December 31, 2003. All of the 68 annuity contracts were issued to residents of the state of Washington, and included: 51 One Life (single) Annuities, Immediate Payments; 16 Two Lives (joint) Annuities, Immediate Payments; and 1 One Life (single) Annuity, Deferred Payment.

Total Net Assets: LBIS' adjusted total of net assets, as determined by this examination, was \$2,252,323. This amount included unrestricted net assets of \$14,856 which was below the required amount of \$500,000. The minimum unrestricted net asset requirements as of December 31, 2003, and December 31, 2002 as well, were not satisfied pursuant to RCW 48.38.010(6). (See "INSTRUCTIONS" No. 2 and No. 3)

Growth of Company: The growth of LBIS for the past five years is reflected in the following exhibits. All information was compiled from LBIS' financial statements as of fiscal years ending June 30. (Please note that this information is provided based on the company's fiscal year-end which is different than the examination as-of date.)

Schedule 1

<u>Fiscal</u> <u>Year</u>	<u>Assets</u>	<u>Liabilities</u>	<u>Total</u> <u>Net Assets</u>	<u>Total Net Assets Allocated Into:</u>		
				<u>Unrestricted</u>	<u>Temporarily</u> <u>Restricted</u>	<u>Permanently</u> <u>Restricted</u>
2003	\$6,225,990	\$3,741,335	\$2,484,655	\$200,679	\$1,304,574	\$979,402
2002	6,454,976	3,872,117	2,582,859	394,628	1,236,982	951,249
2001	6,741,023	3,469,097	3,271,926	865,581	1,492,387	913,958
2000	6,819,674	2,786,967	4,032,707	1,278,556	1,935,116	819,035
1999	8,399,128	3,957,406	4,441,722	1,728,257	2,129,872	583,593

Schedule 2

	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
Total Revenues	\$3,640,976	\$3,351,109	\$3,349,748	\$3,963,465	\$4,790,527
Total Expenses	3,739,180	4,040,176	4,070,531	4,372,480	4,488,454
Excess (deficit) of revenue over expenses	(98,204)	(689,067)	(720,783)	(409,015)	302,073
Net Assets at beginning of year	2,582,859	3,271,926	4,032,707	4,441,722	4,139,649
Adjustment for restatement			(39,998)		
Net assets at end of year	<u>\$2,484,655</u>	<u>\$2,582,859</u>	<u>\$3,271,926</u>	<u>\$4,032,707</u>	<u>\$4,441,722</u>
Number of gift annuity contracts at end of year	68	71	64	63	59

AFFILIATED COMPANIES

LBIS does not have any affiliates.

MANAGEMENT AND CONTROL

Ownership: LBIS is an independent nonprofit corporation. Individual members of the Lutheran Bible Institute of Seattle and Lutheran Trinity College are persons who:

- a) are members of a Christian church,
- b) qualify for membership in accordance with Article VII of the Articles of Incorporation of LBIS, and
- c) have made a contribution recorded within twelve months preceding corporation meetings.

Each individual member has voting privileges at corporation meetings.

Board of Directors: Responsibility for governing the organization is vested in a Board of Directors comprised of twenty-five (25) members including the president of Trinity Lutheran College.

Members of the Board serving LBIS as of Fiscal Year 2003 - 2004 are as follows:

Julius Carroll – Academic
Everett Holum – Academic
David Knode – College Relations
John Foss – Student Life
Betty McNeely – Academic
Susie Tollefson – Academic
Don Benson – Business
Ed Hawxhurst – Business

Lyle Miller – College Relations
Pam Bertani – College Relations
Ruben Duran – College Relations
Guy Ellison – Academic
Pam Fuchs – Student Life
Nancy Gauche – Student Life
Dave Sharkey – Academic
Kris Bjorke – Student Life

Rolle Walker – Business
Sandra Jerke – Business
Dick Lodmill – Business
Norma Larson – College Relations
Chris Boerger – College Relations

Corey Bjertness – Student Life
Dave Sorenson – Student Life
Ernie Fosse – Chairman
John Stamm – President

Officers: The officers of LBIS, elected by the Board of Directors from within its membership, include a Chairman, Vice Chairman, Secretary and Treasurer. These officers, together with the president of Trinity Lutheran College, constitute the legal officers of the corporation pursuant to Article VIII, Section D, of the Articles of Incorporation of LBIS.

Conflict of Interest: LBIS has a Conflict of Interest Policy approved by the Board of Directors on October 18, 2003. The policy requires that each Director disclose in a timely manner to the Chair of the Board any personal, family or other substantial business relationships that reasonably might give rise to a conflict of interest involving the corporation. Also, the Board of Directors requires that each Director annually acknowledge by his or her signature that she or he is in compliance with the letter and spirit of the policy. As of April 19, 2004, Board members have not yet completed or signed the new disclosure forms. The CFO indicated that the completion of these disclosure forms will be discussed at the next board meetings.

CORPORATE RECORDS

The Board of Directors meets at least three times a year to discuss that business which is pertinent to LBIS. Minutes of meetings of directors approve and support organization transactions and events. No exceptions were noted.

STATEMENT OF ACTUARIAL OPINION

A consulting actuary with Milliman USA, Inc., determined the adequacy of the annuity reserves. In the Statement of Actuarial Opinion, the actuary acknowledges that he is a member of the American Academy of Actuaries and meets the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion. His opinion indicates that LBIS' annuity contract reserves meet the requirements of RCW 48.38.020 of the Washington Insurance Code applicable to charitable gift annuities.

ANNUITY ASSETS CUSTODIAL FUNCTION

The assets of the separate reserve fund were held and physically segregated from the other assets of LBIS. Total annuity investments as of December 31, 2003 were \$786,594, and consisted of money market funds, bonds, and stocks. Investments were recorded at fair value.

SUBSEQUENT EVENTS

An Order Suspending Certificate of Exemption Number 137 was signed and entered on April 2, 2004 by the OIC. The basis for the order of suspension is due to LBIS' failure to maintain the minimum unrestricted net assets of five hundred thousand dollars which is a violation of RCW 48.38.010(6). (See "INSTRUCTIONS" No. 2)

ACCOUNTING RECORDS AND PROCEDURES

LBIS classifies its activities by fund and according to donor-imposed restrictions. The three classifications are unrestricted, temporarily restricted, and permanently restricted. Unrestricted funds consist of current operations fund and designated for specific purposes fund. Temporarily restricted funds consist of trusts and annuities, scholarships, special projects, and student loans. Permanently restricted funds are restricted endowment funds.

FINANCIAL STATEMENTS

The following examination financial statements show the financial conditions of LBIS as of December 31, 2003:

Balance Sheet

	<u>Balance Per</u> <u>Annual Report</u>	<u>Adj.</u> <u>Notes</u>	<u>Examination</u> <u>Adjustments</u>	<u>Adjusted</u> <u>Balance</u>
<u>ASSETS</u>				
Current assets	\$2,120,439			\$2,120,439
Receivables	231,940			231,940
Fixed assets (net)	3,315,444			3,315,444
Other assets	1,377,237			1,377,237
Total Assets	<u>\$7,045,060</u>		<u>\$0</u>	<u>\$7,045,060</u>
<u>LIABILITIES</u>				
Accounts payable	\$4,016,647			\$4,016,647
Annuities payable	737,325	Note 1	\$38,765	776,090
Total Liabilities	<u>\$4,753,972</u>		<u>\$38,765</u>	<u>\$4,792,737</u>
Unrestricted	\$14,856			\$14,856
Temporarily restricted	1,269,153	Note 2	(38,765)	1,230,388
Permanently restricted	1,007,079			1,007,079
Total Net Assets	<u>\$2,291,088</u>		<u>\$(38,765)</u>	<u>\$2,252,323</u>
Total Liabilities and Net Assets	<u>\$7,045,060</u>		<u>\$0</u>	<u>\$7,045,060</u>

Adjustment Notes:

Note 1 – To adjust the annuities payable to agree with the calculated statutory annuity reserves. (See “INSTRUCTIONS” No. 1)

Note 2 – To recognize correction to temporarily restricted net assets as a result of the above adjustment. (See “INSTRUCTIONS” No. 1)

Statement of Financial Activity and Changes in Net Assets:

	<u>Balance Per Annual Report</u>	<u>Adj. Notes</u>	<u>Examination Adjustments</u>	<u>Adjusted Balance</u>
Total revenues	\$1,647,031			\$1,647,031
Total expenses	<u>(1,840,598)</u>			<u>(1,840,598)</u>
Increase (decrease) in net assets	(\$193,567)		\$0	(\$193,567)
Net assets at beginning of year	2,484,655			2,484,655
Changes in net assets per examination		Note 3	<u>(38,765)</u>	<u>(38,765)</u>
Net assets at end of year	<u>\$2,291,088</u>		<u>(\$38,765)</u>	<u>\$2,252,323</u>

Adjustment Notes:

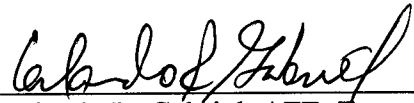
Note 3 – To recognize changes in net assets per examination (See Notes 1 and 2 above).

ACKNOWLEDGMENT

Acknowledgment is hereby made of the cooperation extended to the examiners by the officers of LBIS during the course of this examination.

In addition to the undersigned, Michael V. Jordan, CPA, CFE, MHP, Assistant Chief Examiner, from the Washington State Office of the Insurance Commissioner, participated in the examination and the preparation of this report.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "Orlando R. Gabriel", is written over a horizontal line.

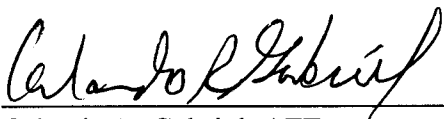
Orlando R. Gabriel, AFE, Examiner-in-Charge
State of Washington

AFFIDAVIT

STATE OF WASHINGTON }
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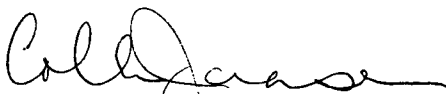
Orlando R. Gabriel, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

He attests that the examination of LBIS was performed in a manner consistent with the standards and procedures required or prescribed by the Washington State Office of the Insurance Commissioner and the National Association of Insurance Commissioners (NAIC).



Orlando R. Gabriel, AFE
Examiner-in-Charge
State of Washington

Subscribed and sworn to before me on this 9th day of November, 2004.



Notary Public in and for the
State of Washington,
Residing at Seattle

